PETITIONER:
BHARAT COMMERCE & INDUSTRIES LTD.

Vs.

RESPONDENT:
THE COMMISSIONER OF INCOME TAX, CENTRAL II

DATE OF JUDGMENT: 05/03/1998

BENCH:
SUJATA V.MANOHAR, D.P. WADHWA

ACT:

HEADNOTE:

JUDGMENT:

[With C.A. Nos. 3355-56/1993]

J U D G M E N T

Mrs. Sujata V. Manohar, J.
C.A. No. 5509 of 1985

The following question was referred to the High Court of Delhi under section 256(1) of the Income-tax Act, 1961, at the instance of the assessee

> "Whether, on the facts and in the circumstances of the case, the claim for deduction of interest levied under section 139 to the extent of Rs. 11,470 and interest levied under section 215 to the extent of Rs. 1,04,339 was rightly rejected as not allowable under section 37 of the Income-tax Act, 1961, for the assessment year 1972-73?"

The High Court has answered the question in the affirmative and in favour of the Revenue. The question pertains to the assessment year 1972-73. The assessee is a limited company manufacturing yarn. It also does some other business activities. The Income-tax Officer at the time of completing the assessment for the assessment year 1972-73 levied interest under section 139 to the extent of Rs. 11,470 and interest under section 215 of the Income-tax Act, 1961, to the extent of Rs. 1,04,339. The assessee claimed deduction of these amounts of interest under section 37 of the Income-tax Act, 1961, in computing its business income. This claim has been rejected.

The assessee contends that the taxes which were payable were delayed and to that extent the assessee's financial resources increased. These increased resources became available for business purposes. Hence the interest which is paid to the Government under sections 139 and 215 represents, in effect, interest on capital that would have been borrowed by the assessee otherwise. Hence these amounts should be allowed as deduction under section 37 as expenses incurred wholly and exclusively for the purpose of its business.

The assessee was required to pay advance tax under section 212 on the basis of his own estimate. Under section 215, if the tax so paid is less than 75 per cent. of the assessed tax, interest as prescribed therein, is payable. It is difficult to see how the interest so paid for not paying the requisite amount of advance tax as prescribed can be considered as expenditure laid out wholly and exclusively for the purpose of business. In the case of *Padmavati Jaikrishna* (*Smt*.) v. *CIT* (Addl.) [1987] 166 ITR 176 (Guj) the assessee borrowed money for the purpose of discharge of her liabilities for the payment of income-tax, wealth-tax and annuity deposit. She paid interest on this borrowed amount. The income earned by the assessee was income from other sources. Hence the allowable deduction would have been under section 57(*iii*). In respect of the payment of annuity deposit this court said that the dominant purpose of making the annuity deposit was not to earn income but to meet the statutory liability of making the deposit. The liability for payment of income-tax and wealth-tax was a statutory liability. Therefore, the expenditure in the form of interest which was paid was not expenditure wholly or exclusively for the purpose of earning income. Hence it could not allowed as a

deduction under section 57(*iii*) of the Income-tax Act, 1961. In the case of *East India Pharmaceutical Works Ltd.* v. *CIT* [1997] 224 ITR 627, this court held that interest on an overdraft for payment of income-tax was not expenditure wholly and exclusively incurred for the purpose of business and was not deductible under section 37 of the Income-tax Act. This court affirmed the decision in the case of *Padmavati Jaikrishna* (*Smt.*) v. *CIT*(*Addl.*) [1987] 166 ITR 176 (SC).

A similar view has been taken by a number of High Courts in earlier decisions. In the case of *Aruna Mills Ltd.* v. *CIT* [1957] 31 ITR 153, the Bombay High Court was concerned with a similar question. It held that the interest which an assessee had to pay under sub-section (7) of section 18A of the Indian Income-tax Act, 1922, for having underestimated the tax payable by him by way of advance tax, cannot be claimed as business expenditure under section 10(2)(*xv*) of the said Act. The court observed that it was difficult to understand how, when a businessman commits default in discharging his statutory obligation, the consequences of that default could constitute an expenditure exclusively incurred for the purpose of his business. The same view was taken in the case of *Orient General Industries Ltd.* v. *CIT* [1994] 209 ITR 490, where the Calcutta High Court has held that interest paid for delay in filing the income-tax return has no connection with the business of the assessee. The assessee does not pay the interest for the purpose of business or for carrying on of the business activity. Hence it is not deductible in computing the income of the assessee. The Calcutta High Court reaffirmed in this case its earlier judgment in *Balmer Lawrie and Co. Ltd.* v. *CIT* [1960] 39 ITR 751 (Cal). The Punjab and Haryana High Court has also taken the same view in *CIT* v. *Oriental Carpet Manufacturers* (*India*) *P. Ltd.* [1973] 90 ITR 373 (P & H) by holding that interest on payment of delayed tax takes colour from the principal amount payable and hence is not deductible. The Madras High Court has also held in *CIT* v. *Sundaram and Co. Pvt. Ltd.* [1964] 52 ITR 763, that interest on money borrowed to pay advance tax is not deductible as business expenditure. This view has been affirmed by this court in *Padmavati Jaikrishna's* case [1987] 166 ITR 176 as well as in *East India Pharmaceutical Works Ltd.'s* case [1997] 224 ITR 627.

The assessee, however, has placed reliance upon a decision of this court in *CIT* v. *Birla Cotton Spinning and Weaving Mills Ltd.* [1971] 82 ITR 166. The assessee in that case had spent money towards expenses in engaging lawyers and conducting proceedings before the Investigation Commission for its case relating to certain assessment years and had also incurred such expenses in courts where the vires of the statute under which the Commission was constituted were challenged. The court allowed the expenses so incurred in connection with the proceedings before the Investigation Commission as deductible expenses while computing the profits of the assessee's business. On the facts of that case the court came to the conclusion that the expenses so incurred were for protection of the assessee's business from any process or proceedings which would have affected its income and profits. Even otherwise the expenditure was incidental to the business and was necessitated or justified by commercial expediency.

The expenses in that case were incurred for a very different purpose from the purpose for which the assessee has paid interest in the present case. When interest is paid for committing a default in respect of a statutory liability to pay advance tax, the amount paid and the expenditure incurred in that connection is in no way connected with preserving or promoting the business of the assessee. This is not expenditure which is incurred and which has to be taken into account before the profits of the business are calculated. The liability in the case of payment of income-tax and interest for delayed payment of income-tax or advance tax arises on the computation of the profits and gains of business. The tax which is payable is on the assessee's income after the income is determined. This cannot, therefore, be considered as an expenditure for the purpose of earning any income or profits. The ratio of *Birla Cotton Mills'* case [1971] 82 ITR 166 (SC) is not applicable in the present case.

Learned counsel for the assessee also relied upon a decision of this court in *Mahalakshmi Sugar Mills Co.* v. *CIT* [1980] 123 ITR 429. The assessee in that case had claimed deduction of interest paid on arrears of sugarcane cess. This was held by this court as a part of the assessee's liability to pay cess and was held to be deductible. The ratio of this judgment also can have no application here. The payment of sugarcane cess is very much a part of the assessee's business expense. Any interest on arrears of cess would, therefore, take colour from the cess which is payable. It is an indirect tax which has to be paid in the course of carrying on business. It is required to be deducted in order to arrive at the net profits of the assessee for the relevant assessment year. We are here not concerned with the payment of any indirect tax which the assessee may have to pay in the course of his business. We are concerned with the tax which was required to be paid after the ascertainment of the net income of the assessee for the relevant assessment year.

Interest which is paid for delayed payment of advance tax on such income cannot be considered as expenditure wholly and exclusively for the purpose of business. Under the Income-tax Act, the payment of such interest is inextricably connected with the assessee's tax liability. If income-tax itself is not a permissible deduction under section 37, any interest payable for default committed by the

assessee in discharging his statutory obligation under the Income-tax Act, which is calculated with reference to the tax on income cannot be allowed as a deduction.

In the present case section 80V of the Income-tax Act is not attracted because section 80V was inserted in the Income-tax Act only with effect from April 1, 1976.

In the premises the High Court has rightly answered the question in favour of the Revenue and against the assessee. The appeal is, therefore, dismissed with costs.
C.A. Nos. 3355-56 of 1993

These appeals relate to the assessment years 1977-78 and 1978-79. The following question was referred to the High Court (see [1993] 200 ITR 232), under section 256(1) of the Income-tax Act, 1961, at the instance of the Revenue (page 233):

> "Whether, on the facts and circumstances of the case and in law, the Tribunal was right in holding that the assessee was not entitled to the deduction of Rs. 2,94,082 in the assessment year 1977-78 and Rs. 43,142 in the assessment year 1978-79 being the interest payable on account of additional liability for income-tax and surtax on account of the disclosure of income made under the Voluntary Disclosure of Income and Wealth Act, 1976, under section 37 or 36(1)(*iii*) of the Income-tax Act, 1961?"

The assessee disclosed certain income under the Voluntary Disclosure of Income and Wealth Act, 1976. As a result the assessee became liable to pay income-tax and surtax. The assessee applied for payment of income-tax and surtax by installments under the provisions of the Voluntary Disclosure of Income and Wealth Act, 1976. The assessee was granted these installments. The assessee was also required to pay interest under section 6 of the said Act for delayed payment of income-tax and surtax. The assessee paid by way of such interest, a sum of Rs. 2,82,106 in the assessment year 1977-78 and a sum of Rs. 36,370 in the assessment year 197879. The claim of the assessee for deduction of these amounts was rejected by the Revenue authorities.

At the instance of the assessee the above question has been raised. The High Court has also answered the question against the assessee. It is the contention of the assessee that instead of taking a loan or withdrawing capital from his business for payment of tax, the assessee obtained installments for payment of tax and was, therefore, required to pay interest. The payment of interest is, therefore, for the purposes of the assessee's business and hence should be allowed as a deduction. The argument is similar to the argument advanced in C.A. No. 5509 of 1985 relating to Bharat Commerce and Industries Ltd. The main point of distinction which the assessee has drawn is that the interest in his case is under the Voluntary Disclosure of Income and Wealth Act, 1976, and hence it should be treated as expenditure incurred for the purposes of the assessee's business.

The Voluntary Disclosure of Income and Wealth Act, 1976— [1976] 102 ITR (St.) 49, is an Act to provide for voluntary disclosure of income and wealth. Section 3 of the Act provides that where any person makes, on or before the prescribed date, as set out in the section, a declaration in respect of any income chargeable to tax under the Indian Income-tax Act for any assessment year for which he has failed to furnish a return under section 139 of the Income-tax Act; or which he has failed to disclose in a return of income; or the assessee makes a declaration of income which has escaped assessment by reason of the omission or failure on the part of such person to make a return or to disclose fully and truly all material facts necessary for his assessment or otherwise; then on the income so disclosed and declared, income-tax shall be charged at the rates specified in the Schedule to the said Act.

Section 4 provides for the manner in which the declaration is to be made and particulars which are to be furnished. Under section 5 income-tax payable under the Act in respect of the voluntarily disclosed income is required to be paid by the declarant before making the declaration and the declaration is required to be accompanied by proof of payment of such tax. Sub-section (2), however, provides that if the Commissioner is satisfied on an application made in this behalf by the declarant, that the declarant is unable, for good and sufficient reasons to pay the full amount of income-tax in respect of the voluntarily disclosed income in accordance with sub-section (1), he may extend the time for payment of the amount which remains unpaid or allow payment by installments if the declarant furnishes adequate security for the payment thereof. However, an amount which is not less than one-half of the amount of income-tax payable in respect of the voluntarily disclosed income has to be paid on or before March 31, 1976, and the remainder, on or before March 31, 1977.

Under section 6, if the amount of income-tax is not paid on or before March 31, 1976, the declarant is liable to pay simple interest at 12 per cent. per annum on the amount remaining unpaid from April 1,

1976, to the date of payment and "the rules made thereunder shall, so far as may be, apply as if the interest payable under this section were interest payable under sub-section (2) of section 220 of the Act (*i.e.,* Income-tax Act, 1961)". The interest, therefore, which is payable for delayed payment of income-tax on the voluntarily disclosed income is of the same nature as interest on income-tax under the Income-tax Act. Payment of such interest cannot be considered as expenditure incurred wholly or exclusively for the purposes of business of the assessee. For the reasons which we have set out above in C.A. No. 5509 of 1985, in the present case also the tax which is required to paid under the Voluntary Disclosure of Income and Wealth Act, 1976, is a tax on the declared income of the assessee which was not disclosed earlier and is disclosed under the said Act. The income-tax is payable by virtue of the said Act. It is nevertheless a tax on income and shares all the characteristics of such tax. When the assessee is liable to pay interest on delayed payment of such tax, it is on account of his not paying income-tax within the prescribed period. We do not see any reason why any distinction can be made between such interest and interest paid under the Income-tax Act, 1961. Both the payments do not have any nexus with the business of the assessee. They are statutory liabilities in respect of the obligations of the assessee which arise under the Income-tax Act and the Voluntary Disclosure of Income and Wealth Act, 1976, after the income of the assessee is determined and/or declared under the said Acts. They cannot be deducted before the determination of such income.

The assessee, however, has drawn our attention to section 80V of the Income-tax Act, 1961, which was in force during the assessment years with which we are concerned. Under section 80V, "In computing the total income of an assessee, there shall be allowed by way of deduction any interest paid by him in the previous year on any money borrowed for the payment of any tax due from him under this Act". Learned counsel for the respondent submitted that section 80V will apply only to the payment of any tax under the Income-tax Act of 1961. It will not apply to payment of income-tax under the Voluntary Disclosure of Income and Wealth Act, 1976. We need not dwell on this submission because, even if we assume that section 80V does apply it can apply only if the assessee has borrowed any money for payment of any tax and has paid interest in the relevant previous year on such borrowed money. In the present case, the assessee has not borrowed any money for the purpose of paying tax; nor has he paid any interest to any third party for such borrowing. The contention of the assessee seems to be, that he had avoided borrowing money for payment of tax by obtaining installments from the Department and paying interest. Therefore, the payment of interest should be considered as equivalent to his paying interest on borrowed money for payment of tax. The submission has to be stated to be rejected. Obtaining installments from the Department and paying interest cannot be considered as equivalent to borrowing moneys from a third party for payment of tax and paying interest on such borrowed money. The assessee's argument, if taken to its logical conclusion, would amount to saying that the assessee had, in effect, borrowed moneys from the Income-tax Department, to pay tax for which he was paying interest to the Income-tax Department. Such is clearly not the case, as it cannot be.

The assessee has placed reliance on a decision of the Andhra Pradesh High Court in the case of *CIT* v. *Bakelite Hylam Ltd.* [1988] 171 ITR 583. In the case before the Andhra Pradesh High Court the assessee had taken certain amounts from his overdraft account to pay income-tax. The interest payable on the amount so withdrawn was held deductible under section 80V. This decision has no application to the facts of the present case where the assessee has not borrowed any moneys for payment of income-tax. Section 80V is not attracted in the present case.

The assessee has strongly relied upon a decision of the Gujarat High Court in the case of *C.J. Patel and Co.* v. *CIT* [1986] 158 ITR 486. The case before the Gujarat High Court was a case where the assessee had made a disclosure under the Voluntary Disclosure Scheme. Instead of making payment of tax a bank guarantee was furnished to the Department and commission was paid to the bank for obtaining the bank guarantee. A question arose whether this commission which was paid to the bank by the assessee was allowable as a deduction. The Gujarat High Court purported to distinguish the earlier judgments where interest paid on delayed payment of tax was held as not deductible. The Gujarat High Court said that payment of interest for delayed payment of tax or payment of interest on moneys borrowed from third parties for payment of tax may be inadmissible. But such payments are not similar to the payment which an assessee makes to the bank as commission for obtaining a bank guarantee for securing the payment of tax. The Gujarat High Court has not held that payment of interest on delayed payment of tax is an expense incurred wholly for the purposes of the assessee's business. It has, however, distinguished commission on bank guarantee from interest on money borrowed for payment of tax. The above case does not, therefore, help the assessee in the present case. We need not, therefore, examine the correctness or otherwise of the judgment of the Gujarat High Court.

It cannot be said, in the present case, that the payment of interest is in any way an expense incurred wholly or exclusively for the purpose of the assessee's business. Nor is it a payment made for the

purpose of preserving and protecting the assessee's business as in the case of *Birla Cotton Mills* [1971] 82 ITR 166 (SC).

Apart from section 37, the assessee had also pressed into service section 36(1)(*iii*) which permits deduction in respect of the amount of interest paid in respect of capital borrowed for the purposes of the assessee's business or profession. For the reasons set out earlier, the claim for deduction under section 36(1)(*iii*) is also misconceived just as the assessee's claim under section 37 is misconceived.

In the premises, the question raised has to be answered in favour of the Revenue and against the assessee. The appeals are, therefore, dismissed with costs.